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Decision 01-12-025 December 11, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into Implementation of Public Utilities Code Section 390.	Rulemaking 99-11-022 (Filed November 18, 1999)

ORDER MODIFYING DECISION (D.) 01-03-067 AND DENYING REHEARING, AS MODIFIED

In 1996, as part of the legislation for restructuring California's electric industry, the Legislature enacted Public Utilities Code section 390. Section 390 prescribed the methodology for determining energy prices to pay non-utility power generators. Pursuant to the requirements of section 390(b), the Commission issued Decision (D.) 96-12-028, which adopted a transitional formula for each utility to calculate its short run avoided cost (SRAC) payments to qualifying facilities (QFs). This transitional formula included a utility-specific "factor" which was designed to relate SRAC prices to gas border prices for each utility.

On July 28, 2000, Southern California Edison Company (Edison) filed a petition to modify its factor from a fixed amount to one which would be adjusted monthly. Edison claimed that because of lower intrastate transportation costs, the relationship of its avoided costs and gas border prices was no longer reflected in the fixed factor. In its August 28, 2000, comments on Edison's petition for modification, the Office of Ratepayer Advocates (ORA) recommended that the Commission also review the gas border price indices used in the SRAC formulas applicable to the utilities. ORA asserted that the Commission should not use the gas price indices for Topock deliveries at the Arizona/California border, as it believed that index was no longer robust.

On March 28, 2001, the Commission issued Decision (D.) 01-03-067. In D.01-03-067, the Commission modified the transitional SRAC formula by: 1) replacing Edison's fixed factor with dynamic formula and 2) establishing a procedure to replace the Topock index with the Malin index. The Commission also ordered the utilities to make payments to QFs for energy deliveries within 15 days after the end of each billing period and informed the utilities that a significant penalty would be assessed for failing to make timely payments.

On April 27, 2001, Edison, Pacific Gas and Electric Company (PG&E) filed applications for rehearing.[1] Edison asserts in its rehearing application that the Commission: 1) failed to order retroactive application of the modified SRAC formula; 2) needs to clarify why the Malin indices were adopted; and 3) needs to clarify the accelerated payment provisions and eliminate the penalty provision for failing to make timely payments. In its application for rehearing, PG&E contends that: 1) the Commission unlawfully amended its contracts with QFs by accelerating the payment schedule; 2) the Commission needs to specify that the "benchmark" Consumer Transition Price (CTP) does not represent rates that PG&E must actually pay to QFs; and 3) because Federal bankruptcy law prohibits payments for any pre-petition liability without approval of the Bankruptcy Court, the Commission could not assess a penalty should it fail to make timely payments on deliveries it received from the QFs between March 27, 2001 and April 6, 2001.

[1] Applications for rehearing were also filed by Calpine Corporation, Caithness Energy, Mega Renewables, Mega Hydro I, Central Hydroelectric Corporation, Tracteble Power, Inc. et al, CE Generation, Cogeneration Association of California, California Cogeneration Council, Independent Energy Producers Association and County of Los Angeles (collectively, the "QF parties"). Because the utilities raise different issues than those raised by the QF parties, this decision only considers the rehearing applications filed by Edison and PG&E. The rehearing applications filed by the QF parties will be addressed in a subsequent order.

The California Cogeneration Council (CCC), Caithness Energy (Caithness), and Tractebel Power, Inc./Tractebel Energy Marketing, Inc. (Tractebel) filed responses to Edison's rehearing application on May 14, 2001.

I. RETROACTIVE APPLICATION OF THE MODIFIED SRAC FORMULA

In D.01-03-067, we ordered that, effective March 27, 2001, payments to QFs be based on the modified SRAC formula adopted in the decision. (D.01-03-067 at 35 (OP 8).) Edison contends that failure to apply this modified formula retroactively, for the period December 2000 through March 2001, constitutes legal error. It asserts that the facts which support a finding that the factor and gas indices need to be adjusted prospectively also support retroactive application. (Edison Application at 6.) Further, it maintains that, since the SRAC methodology used during that period overstated its avoided costs, the Commission's implementation of the methodology was in violation of the Public Utility Regulatory Policies Act of 1978 (PURPA). (*Id*. at 8.) CCC, Caithness, and Tractebel filed responses opposing Edison's rehearing application.

Upon consideration of the arguments presented by Edison, we find no error in only applying the modified SRAC formula prospectively. First, nothing in the record supports a finding that retroactive application of the formula is warranted. In fact, this issue was not raised, and parties have not had an opportunity to comment on the issue. Additionally, the FERC's regulations provide that "[i]n the case in which the rates for purchases are based upon estimates of avoided costs over the specific term of the contract or other legally enforceable obligation, the rates for such purchases do not violate this subpart if the rates for such purchases differ from avoided costs at the time of delivery." (18 C.F.R. § 292.304(b)(5).) This suggests that the Commission can, consistent with PURPA, provide for avoided costs that differ from the utility's, so long as those costs are derived from consistent application of a formula. Therefore, it is not a *per se* violation of PURPA if the SRAC formula overstated Edison's avoided costs during that period. Finally, our decision whether to modify the SRAC formula is discretionary, and there is no requirement that we must act by a certain date.

While we do not retroactively apply the modified SRAC formula at this time, we remind parties that we have legal authority to adjust SRAC prices to ensure compliance with section 390. In D.96-12-028, we determined that the Topock indices used to calculate the SRAC price were robust and therefore met the market-based pricing requirement under section 390. (D.96-12-028, 69 Cal.P.U.C. 2d at 552.) Evidence presented in this proceeding led us to conclude that the Topock indices were no longer sufficiently robust to be utilized in the SRAC formula on a prospective basis. (D.01-03-067 at 33 (COL 33).) However, we may also consider whether this lack of robustness resulted in prior SRAC price postings which did not meet the requirements of section 390.

Although we do have authority to consider retroactive adjustment of SRAC prices, we decline to do so in this instance. A decision to consider retroactive adjustment of SRAC prices could increase the uncertainty in the current QF market, since many QFs appear to have continued operations with the expectation that they would eventually be "made whole" by the utilities. Moreover, investigation into the robustness of the various indices could require significant commitment of Energy Division staff due to the potential complexity involved and further strain the Commission's current resources. Furthermore, we have previously declined to allow retroactive downward adjustments of posted prices. (*See, e.g., Biennial Resource Update Plan [D.96-07-026]* (1996) 66 Cal.P.U.C. 2d 780; *Order Instituting Ratemaking No. 2 [D.82-12-120]* (1982) 10 Cal.P.U.C. 2d 553.) While we believe this situation is distinguishable, we believe that the need to provide pricing certainty for QFs, which was articulated in those decisions, also exists in this case. Therefore, under these circumstances, we do not believe retroactive adjustment would be in the public interest. Finally, it appears that the factors contributing to the aberrations in the Topock indices no longer exist, and the indices are once again sufficiently robust. We believe that the current proceeding in this docket will adequately address methods to identify and respond to future aberrations in the marketplace. Consequently, for these reasons, we have decided to not consider adjustment of any SRAC prices prior to March 2001.

II. THE MALIN INDICES

In D.01-03-067, we ordered that the Topock indices be replaced with the Malin indices (plus transportation) until further notice. In its rehearing application, Edison requests that the Commission clarify why the Malin indices were adopted to replace the Topock indices. (Edison Application at 9.)

Pursuant to Public Utilities Code section 1732, the "[t]he application for a rehearing shall set forth specifically the ground or grounds on which the applicant considers the decision or order to be unlawful." Edison has not challenged the lawfulness of the Commission's decision to use the Malin indices, but is merely seeking clarification. Therefore, it has failed to meet the requirements of section 1732, and no clarification shall be made at this time.[2]

III. ACCELERATED PAYMENT SCHEDULE AND PENALTY

In D.01-03-067, we noted that due to disputes between the utilities and the QFs over the amounts due for energy delivered between November 2000 and March 2001, many QFs had not been paid for some period of time. Therefore, we ordered the utilities to pay the QFs for energy delivered within 15 days after the end of the billing period. The utilities were also informed that if they failed to make payments in a timely fashion, they would be subject to a penalty equal to the amount of the payment owed.

PG&E contends that under PURPA, the Commission may not interfere with the terms of its contracts with the QFs and that doing so is an

[2] We note that the QF parties have challenged the lawfulness of the Commission's decision to use the Malin index in their rehearing applications. Consequently, any clarification regarding our decision to use the Malin indices shall be made when we consider the arguments raised by the QF parties.

unlawful impairment of contract based on *Freehold Cogeneration Associates L.P. v. Board of Commissioners of New Jersey* (3d Cir. 1995) 44 F.3d 1178, and the Contract Clause (U.S. Const., Art. 1, sec. 10, clause 1). (PG&E Application at 3). PG&E further asserts that the proposed penalty is unduly punitive and, therefore, must be eliminated. Finally, PG&E notes that Federal bankruptcy law prohibits payments for any pre-petition liability without approval of the Bankruptcy Court. Therefore, PG&E asserts that it cannot be assessed a penalty for failing to pay QFs for any deliveries made between March 27, 2001, through April 6, 2001.

PG&E's claims regarding accelerated payment are without merit. In this instance, our order is pursuant to the Commission's obligation to assure adequate service by the utilities. (*See, e.g.*, Pub. Util. Code §§ 451, 701, 761.) In *Freehold*, the Third Circuit Court of Appeals stated that although states have broad authority to implement PURPA, they are prohibited from "utility-type regulation" of QF contracts. (*Freehold*, 44 F.3d at 1192-93.) It is unlikely that an order to accelerate payment by the utilities would be considered a form of utility regulation over the QFs. Thus, PG&E's PURPA claims do not prevail.[3] Additionally, although our order for accelerated payment affects PG&E's contracts with its QFs, we have acted within our authority under the Contract Clause. Courts have recognized that, notwithstanding the Contract Clause, states "possess authority to safeguard the vital interests of its people." (*Home Bldg. & Loan Assn. v. Blaisdell* (1934) 290 U.S. 398, 434.) In balancing the Contract Clause against the State's interest in exercising its police power, courts look at whether the act was: 1) an emergency measure, 2) for the protection of a basic societal interest, rather than particular individuals, 3) appropriate to address the emergency, 4) reasonable, and 5) limited to the duration of the emergency. (*Id.* at 444-47.)

[3] Only PG&E's PURPA claims are addressed here. This decision does not in any manner prejudge the PURPA challenges raised by the QF parties in their rehearing applications.

Our order for accelerated payment meets the *Home Building* test. Evidence in the record shows that some of the QFs expressed concerns about impending financial hardship, as they had not received payment for energy delivered for several months. Comments filed by some QF parties noted that continued non-payment by the utilities could result in their being forced to reduce output. The decision notes that "energy from QFs is an essential part of the state's electric supply." (D.01-03-067 at 25.) Therefore, an order requiring the utilities to pay the QFs in a timely manner would be considered an appropriate way to address these concerns. Our determination that the payment term of 30 days after the billing period should be accelerated to 15 days is also reasonable. Indeed, the utilities have not demonstrated that the shortened time period has substantially affected their obligations under the contracts nor caused any undue hardship on them. Finally, language in the decision indicates that this accelerated payment period would be for limited duration. (*Id*.)

Edison requested certain clarification of the decision regarding the accelerated payment period. (Edison application at 11.) However, there is no allegation of legal error. As discussed previously, this request fails to meet the requirements of section 1732. Consequently, we decline to make any clarifications at this time.

Upon consideration of the arguments raised by PG&E and Edison, we agree that the penalty provision is not necessary at this time. Therefore, we modify D.01-03-067 to eliminate references to the penalty. However, the utilities are reminded that the Commission is authorized to impose penalties for failing to comply with our orders. Therefore, should any utility fail to make timely payment, it will be subject to an order to show cause why a penalty should not be imposed.

IV. THE CONSUMER TRANSITION PRICE

D.01-03-067 established a reasonableness benchmark called the Consumer Transition Price (CTP). (D.01-03-067 at 21.) This benchmark was a general pricing goal for the average cost of QF production. However, the decision clearly noted that the CTP was neither a cap nor a ceiling on payments.

PG&E asserts that the decision must clarify that CTP does not represent actual payments by utilities to QFs and that it cannot be used as the basis for calculating the California Procurement Adjustment (CPA). It appears to believe that the Commission has failed to comply with PURPA unless this clarification is made. We are unsure of the basis for this argument. The decision clearly states that the CTP is a "reasonableness benchmark . . . to express our expectations that under PURPA payments to QFs be just and reasonable for electric consumers." There is no reference to the CPA in this decision. In fact, the CPA methodology, which was adopted in D.01-04-005, does not use the CTP in estimating QF prices. That decision clearly notes that the CPA is a benchmark and does not reflect actual utility costs. Since the CTP is not the basis for calculating the CPA, PG&E's assertion is without merit.

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Therefore **IT IS ORDERED** that

1. D.01-03-067 is modified as follows:

   a. The last sentence on page 25 shall be deleted.

   b. On page 34, Conclusion of Law 22 shall be deleted.

   c. On page 35, Ordering Paragraph 11 shall be deleted and the subsequent Ordering Paragraphs renumbered accordingly.

2. The rehearing applications filed by Pacific Gas and Electric Company and Southern California Edison Company of D.01-03-067, as modified herein, are denied.

This order is effective today.

Dated December 11, 2001 at San Francisco, California.

LORETTA M. LYNCH
President
HENRY M. DUQUE
RICHARD A. BILAS
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners